



Auditor-General of South Africa

Mpofana Municipality
Audit report 2017-18

Report of the auditor-general to the KwaZulu-Natal Provincial Legislature and the council on Mpofana Municipality

Report on the audit of the financial statements

Disclaimer of opinion

1. I was engaged to audit the financial statements of the Mpofana Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2018, the statement of financial performance, statement of changes in net assets, and cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. I do not express an opinion on the financial statements of the municipality. Because of the significance of the matters described in the basis for disclaimer of opinion section of this auditor's report, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for disclaimer of opinion

Revenue from exchange transactions - Service charges

3. I was unable to obtain sufficient appropriate audit evidence for service charges due to the status of the accounting records. Service charges revenue on the general ledger and the trial balance did not reconcile to the financial statements. In addition, journals recorded on the general ledger were not supported. I could not confirm the recorded revenue by alternative means. Consequently, I was unable to determine whether any further adjustment was necessary to service charges stated at R61,87 million, receivables stated at R28,78 million and debt impairment stated at R16,26 million in note 20, note 9 and note 32 respectively. Additionally, there was a resultant impact on the deficit for the period and on the accumulated surplus.

Receivables

4. I was unable to obtain sufficient appropriate audit evidence for receivables from exchange and non-exchange transactions due to the poor status of the accounting records. The amounts per the debtors age analysis for receivables did not agree to the financial statements and the provision for bad debt was not supported by detailed listings. In addition, there were misclassifications and differences between the amounts in the general ledger and the amounts disclosed in the financial statements for exchange and non-exchange receivables and comparatives did not agree to the prior year audited amounts. I could not confirm receivables from exchange and non-exchange transactions by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to receivables stated at R47,14 million (2017: R41,60 million) in note 9 and note 10 to the financial statements and debt impairment stated at R16,26 million in note 32 to the financial statements. Additionally, there was a resultant impact on the deficit for the period and on the accumulated surplus.

Property, plant and equipment

5. The municipality did not record and depreciate property, plant and equipment, as required by GRAP 17, *Property, plant and equipment*. Depreciation was incorrectly calculated and was also calculated on leased assets that were returned to the supplier during the year. In addition, recorded amounts for work in progress did not agree to the supporting invoices and projects under construction were not recorded on the schedule of work in progress. Furthermore, supporting documents were not provided for changes in accounting estimates recorded on the fixed asset register. I was unable to determine the impact of this misstatement as it was impracticable to do so for work in progress stated at R18,73 million (2017: R 7,14 million) and depreciation stated at R16,98 million (R12,86 million) in note 4 to the financial statements. Additionally, there was a resultant impact on the deficit for the period and on the accumulated surplus.

VAT Receivable

6. I was unable to obtain sufficient appropriate audit evidence for the VAT receivable as the municipality did not have adequate systems to record VAT transactions. Differences were noted between the control account, monthly reconciliations and the VAT returns. I could not confirm the VAT receivable by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to the VAT receivable stated at R6,03 million in note 11 to the financial statements.

Payables from exchange transactions

7. I was unable to obtain sufficient appropriate audit evidence for payables from exchange transactions due to the status of the accounting records. Payables were not supported by appropriate schedules or registers and differences were noted between the general ledger and the financial statements. Furthermore, debtor payments received in advance did not reconcile with the debtors age analysis and invalid advance payments were identified. I could not confirm the payables from exchange transactions by alternative means. I was unable to determine the impact of this misstatement as it was impracticable to do so for the payables stated at R114,32 million in note 17 to the financial statements.

Provisions

8. I was unable to obtain sufficient appropriate audit evidence that the leave pay included in provisions had been properly accounted for, due to the status of accounting records. Leave balances were not supported by leave files and errors were identified on calculations of leave amounts. I was unable to determine the impact of this misstatement as it was impracticable to do so for the leave provision stated at R3,18 million (2017: R3,22 million) in note 16 to the financial statements. Additionally, there was an impact on the deficit for the period and on the accumulated surplus.

Unspent conditional grants and receipts

9. I was unable to obtain sufficient appropriate audit evidence for unspent conditional grants and receipts due to the status of the accounting records. Unspent conditional grants and receipts on the general ledger and the trial balance did not reconcile to the financial statements. In addition, journals recorded on the general ledger were not supported. I could not confirm the recorded liability by alternative means. Consequently, I was unable to determine whether any

further adjustment was necessary to unspent conditional grants and receipts stated at R16,62 million and government grants and receipts stated at R48,01 million in note 15 and note 26 respectively. Additionally, there was a resultant impact on the deficit for the period and on the accumulated surplus.

Property rates – penalties imposed

10. The municipality did not measure and record items that meet the definition of revenue in accordance with GRAP 9, Revenue from exchange transactions. The municipality did not calculate and charge penalties on debtors whose accounts were handed over as required by the municipal property rates policy. I was unable to determine the impact of this misstatement as it was impracticable to do so for property rates – penalties imposed and receivables from non-exchange transactions stated at R28,78 million in note 9 to the financial statements. Additionally, there was an impact on the deficit for the period and on the accumulated surplus.

Licences and permits

11. During 2017, I was unable to obtain sufficient appropriate audit evidence for licences and permits and to confirm the revenue by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to licences and permits stated at R3,20 million. My audit opinion on the financial statements for the period ended 30 June 2017 was modified accordingly. My opinion on the current year financial statements was also modified because of the possible effect of this matter on the comparability of the licences and permits for the current period.

General expenses

12. General expenses were not recorded and disclosed or presented by nature as required by GRAP 1, *Presentation of financial statements*. Repairs and maintenance as well as grant expenditure was not presented by nature on the financial statements. Expenditure recorded in the general ledger did not agree to supporting invoices. I was unable to determine the impact of these misstatements as it was impracticable to do so for general expenses stated at R35,10 million (2017: R30,36 million) in note 35 to the financial statements. Additionally, there was an impact on the deficit for the period and on the accumulated surplus.

Revenue and expenditure

13. The municipality did not disclose the reclassifications of revenue and expenditure as required by GRAP 1, *Presentation of Financial Statements*. The nature, amounts and the reasons for the reclassifications of revenue and expenditure were not disclosed in the financial statements. Consequently, I was unable to determine whether any further adjustments were necessary to revenue and expenditure disclosed in the financial statements.

Change in accounting estimates

14. The municipality did not disclose particulars of the change in accounting estimates relating to property, plant and equipment as required by GRAP 3, *Accounting policies, changes in accounting estimates and errors*. The nature and amounts of the changes in accounting estimates that were recorded on property, plant and equipment were not disclosed in the notes to the financial statements.

Irregular expenditure

15. The municipality did not include all instances of irregular expenditure in the notes to the financial statements, as required by section 125(2)(d) of the MFMA. This was due to payments made in contravention of the supply chain management requirements. I was unable to determine the impact of this misstatement as it was impracticable to do so for irregular expenditure stated at R48,72 million (2017: R32,50 million) in note 47 to the financial statements.

Unauthorised expenditure

16. I was unable to obtain sufficient appropriate audit evidence that the unauthorised expenditure disclosed had been properly accounted for, due to the status of accounting records. The unauthorised expenditure recorded did not reconcile to the supporting schedules. I was unable to confirm this by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the unauthorised expenditure stated at R133,17 million in note 45 to the financial statements.

Commitments

17. The municipality did not disclose all contractual commitments in accordance with GRAP 1, *Presentation of financial statements*. As the municipality did not maintain adequate records of contract amounts and payments made we could not confirm the commitments amount disclosed. Recorded commitment balances did not agree to supporting records. I was unable to determine the full extent of this misstatement for commitments as it was impracticable to do so. Consequently, I was unable to determine whether any adjustments were necessary to commitments stated at R48,37 million in note 38 to the financial statements.

Electricity losses

18. I was unable to obtain sufficient appropriate audit evidence for electricity losses, due to inadequate systems and processes for the recording and monitoring of these losses. Billed electricity units were not supported by adequate accounting records. I was unable to confirm the electricity losses by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to electricity losses stated at R11,59 million in note 50 to the financial statements.

Material uncertainty relating to going concern

19. I draw attention to the matter below. My opinion is not modified in respect of this.
20. I draw attention to note 43 to the financial statements, which indicates that unspent grants are not fully cash backed and current liabilities exceeded the current assets. As stated in note 43, these events or conditions, along with the other matters as set forth in note 43, indicate that a material uncertainty exists that may cast significant doubt on the municipality's ability to continue as a going concern.

Emphasis of matters

21. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

22. As disclosed in note 41 to the financial statements, the corresponding figures for 30 June 2017 were restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2018.

Fruitless and wasteful expenditure

23. As disclosed in note 46 to the financial statements, the municipality incurred fruitless and wasteful expenditure of R2,13 million, due to interest and penalties on late payments to suppliers. Fruitless and wasteful expenditure of R2,70 million that was incurred in the previous years was not investigated.

Other matter

24. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Unaudited disclosure notes

25. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, we do not express an opinion on it.

Responsibilities of the accounting officer for the financial statements

26. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and Dora, and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
27. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

28. My responsibility is to conduct an audit of the financial statements in accordance with the International Standards on Auditing and to issue an auditor's report. However, because of the matters described in the basis for disclaimer of opinion section of this auditor's report, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.
29. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and the ethical requirements that are relevant to my audit of the separate financial statements in South

Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.

Report on the audit of the annual performance report

Introduction and scope

30. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for the selected development priority presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
31. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
32. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priority presented in the annual performance report of the municipality for the year ended 30 June 2018:

Development priority	Pages in the annual performance report
Development priority 2 – basic service delivery	x – x

33. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

I did not raise any material findings on the usefulness and reliability of the reported performance information for this development priority.

Other matters

34. I draw attention to the matters below.

Achievement of planned targets

35. The annual performance report on pages ... to ... includes information on the achievement of planned targets for the year.

Adjustment of material misstatements

36. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of basic service delivery development priority. As management subsequently corrected the misstatements, I did not raise any material findings on the usefulness and reliability of the reported performance information.

Report on the audit of compliance with legislation

Introduction and scope

37. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.
38. The material findings on compliance with specific matters in key legislation are as follows:

Annual financial statements

39. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of non-current assets, current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements of non-current assets, current assets, liabilities, revenue, expenditure and disclosure items and supporting records that could not be provided resulted in the financial statements receiving a disclaimer audit opinion.

Expenditure management

40. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
41. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The full extent of the irregular expenditure could not be quantified as indicated in the basis for qualification paragraph. The majority of the irregular expenditure was caused by supply chain management processes not followed.
42. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R2,13 million as disclosed in note 46 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by interest and penalty charges for late payments to suppliers.

43. Reasonable steps were not taken to prevent unauthorised expenditure, as required by section 62(1)(d) of the MFMA. The full extent of the unauthorised expenditure could not be quantified as indicated in the basis for qualification paragraph. The majority of the disclosed unauthorised expenditure was caused by overspending the adjustment budget.

Revenue management

44. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
45. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

Asset management

46. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Procurement and contract management

47. Some of the bid documentation for procurement of commodities designated for local content and production, did not stipulated the minimum threshold for local production and content as required by the 2017 preferential procurement regulation 8(2).
48. Some of the commodities designated for local content and production, were procured from suppliers who did not submit a declaration on local production and content as required by the 2017 preferential procurement regulation.
49. Some of the commodities designated for local content and production, were procured from suppliers who did not meet the prescribed minimum threshold for local production and content, as required by the 2017 preferential procurement regulation 8(5).
50. Some of the contracts were awarded to bidders based on preference points that were not allocated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its regulations. Similar non-compliance was also reported in the prior year.
51. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).

Consequence management

52. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) of the MFMA.
53. Irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.

Other information

54. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report and the selected development priority presented in the annual performance report that have been specifically reported in this auditor's report.
55. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
56. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected development priority presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
57. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate. However, if it is corrected this will not be necessary.

Internal control deficiencies

58. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it.
59. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the disclaimer of opinion and the findings on compliance with legislation included in this report.
60. Leadership did not adequately oversee financial reporting and compliance with legislation. In this regard, leadership did not ensure that effective measures were taken to address previous year's audit findings.
61. Management did not implement a proper records management system to maintain documents supporting non-current assets, current assets, liabilities, revenue, expenditure, disclosure items and journals recorded in the general ledger.

Other reports

62. I draw attention to the following engagement conducted by various parties that had, or could have, an impact on the matters reported in the municipality's financial statements, reported performance information, compliance with applicable legislation and other related matters. These reports did not form part of my opinion on the financial statements compliance with legislation.

63. An independent consultant investigated an allegation of possible financial misconduct at the request of the KwaZulu-Natal Department of Cooperative Governance and Traditional Affairs, which covered the period 01 February 2011 to 30 June 2018. The investigation concluded on 01 November 2018 and recommends disciplinary hearings and criminal proceedings against the parties involved.

Auditor General
Pietermaritzburg

30 November 2018



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence